No. 90-504

(4)

Supreme Court, U.S.
FILED
OCT 19 1990
JOSEPH F. SPANIOL, JR.
CLERK

In The

Supreme Court of the United States

October Term, 1990

FLEET FACTORS CORP.,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Eleventh Circuit

BRIEF OF AMICUS CURIAE, AMERICAN COLLEGE OF REAL ESTATE LAWYERS, IN SUPPORT OF PETITIONER

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BRIEF AS AMICUS CURIAE

INTEREST OF AMICUS CURIAE

The American College of Real Estate Lawyers is a non-profit corporation organized for the purpose of gathering together lawyers distinguished for their expertise and high standards of professional and ethical conduct in the practice of real estate law, in order, *inter alia*, to improve and reform real estate law and practice and to speak upon matters of interest and importance to real estate law and practice. College members are required to have concentrated their practice in real estate law for a period of not less than ten years. Additional requirements established by the Board of Governors include a demonstrated willingness to devote time to improving real property law, by writing, teaching or participating in organized bar projects. The College has over 700 members from every state and the District of Columbia. They represent owners, borrowers, lenders, purchasers, sellers, institutional investors, developers, in short, those regularly engaged in both pre- and post-closing activities relating to consummating, monitoring in a meaningful way, and working out secured loan transactions involving both real and personal property.

The College is interested in this case because it substantially impacts secured creditor investment and loan portfolio administration decisions. The decision below established a new classification of liability for secured creditors that precludes consistent, uniform and coherent loan administration and loan initiation decisions.

The Eleventh Circuit has established a new test as to when one holding indicia of ownership primarily to protect his security interest participates in management sufficiently so as to lose the statutory exemption afforded secured creditors under CERCLA.

Because of the hundreds of thousands of secured lending transactions each year throughout the country, it is imperative that this unwarranted standard not be permitted to stand. The College believes that this Court's review of the decision below is essential if the dual goals of environmental due diligence and making credit available to the nation's borrowers are to be met.

The College believes that clarification by this Court of the circumstances whereby a secured creditor may incur liability under the Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA") is essential in order to eliminate the chilling effect of the decision below on the availability of credit to the nation's borrowers. For that reason, the College submits this brief in support of the Petitioner.

SUMMARY OF ARGUMENT

The Eleventh Circuit in the case at bench departed from established district court precedent and a reasonable construction of CERCLA's secured creditor exemption when it formulated a new standard for determining when a secured creditor participates in management so as to become liable under CERCLA as an owner or operator. That court held that it is not necessary for a secured creditor actually to involve itself in the borrower's day-

to-day operations or to participate in management decisions relating to hazardous waste in order to be liable. Rather, the court held that a secured creditor will be liable if an inference can be drawn from the secured creditor's involvement with the borrower's business that, if the secured creditor so chose, it could affect its borrower's hazardous waste disposal decisions, or, as the court put it another way, that the secured creditor will be liable if it has the capacity to influence the borrower's treatment of hazardous waste, even if there is absolutely no proof whatsoever that it exercised that capacity or that its management activities, indeed, resulted in influencing the borrower's treatment of hazardous waste.

This radically expansive new threshold for the exemption's availability has sent a shock wave throughout the country because, to say the least, the distinction between those lending activities that CERCLA exempts and those that will subject a secured creditor to liability are now virtually indistinguishable in the Eleventh Circuit.

Moreover, because of the Ninth Circuit's subsequent decision in *In re Bergsoe Metal Corp.*, 910 F.2d 688 (9th Cir. 1990), which directly conflicts with the case at bench, lenders and borrowers, large and small, throughout the county, are faced with a Hobson's choice regarding what they can or should do or avoid in order to qualify for the protection intended by Congress. Clear, predictable, fair, uniform and rational rules should exist for borrowers and lenders affected by the broad reach of CERCLA liability.

The decision below would inject an unwarranted new standard as to when a secured creditor may be liable for

CERCLA response costs, a standard well beyond that intended by Congress. It is an extremely important issue that requires resolution by this Court.

ARGUMENT

I. THE ELEVENTH CIRCUIT ERRED IN HOLDING THAT A NON-FORECLOSING SECURED CREDITOR MAY INCUR SECTION 9607 (a) (2) CERCLA LIABILITY MERELY ON THE BASIS OF A CAPACITY TO INFLUENCE A BORROWER'S TREATMENT OF HAZARDOUS WASTES.

A. The Eleventh Circuit has created a standard for CERCLA liability inconsistent with and exceeding the statutory liabilities established by CERCLA.

To the extent that any "safe harbor" from CERCLA liability exists, it is embodied in the secured creditor exemption construed by the Eleventh Circuit in *Fleet Factors Corp. v. United States of America*, 901 F.2d 1550 (11th Cir. 1990), the Ninth Circuit in its more recent *Bergsoe* decision, and earlier district court decisions which generally stand for the proposition that lenders are not liable for cleanup costs so long as they do not foreclose and do not participate in the day-to-day operations of the secured facility. *See United States v. Mirabile*, No. 84-2280 (E.D. Pa. Sept. 6, 1985); *United States v. Maryland Bank & Trust Co.*, 632 F. Supp. 573 (D. Md. 1986); and *Guidice v. BFG Electroplating & Mfg. Co.*, 732 F. Supp. 556 (W.D. Pa. 1989).

Prior to *Fleet*, the cases had held that the management activities of secured creditors must be relatively

significant before the CERCLA exemption would not be available. In stating that "the critical issue is whether *Fleet* participated in management sufficiently to incur liability under the statute," and that "In order to achieve the 'overwhelming remedial' goal of the CERCLA statutory scheme, ambiguous statutory terms[1] should be construed to favor liability for the costs incurred by the government in responding to the hazards at such facilities," the court held that:

> Under the standard we adopt today, a secured creditor may incur . . . liability, without being an operator, by *participating* in the *financial* management of a facility *to a degree indicating* a *capacity to influence* the corporation's treatment of hazardous wastes. It is not necessary for the secured creditor *actually* to involve itself in the *day-to-day* operations of the facility in order to be liable – although such conduct will *certainly* lead to the loss of the protection of the statutory exemption. Nor is it necessary for the secured creditor to *participate* in management decisions relating to hazardous waste. Rather, a secured creditor will be liable if its *involvement* with the management of the facility is *sufficiently broad* to *support* the *inference* that it *could* affect hazardous waste disposal decisions *if it so chose* . . . . Nothing in our discussion should preclude a secured creditor from *monitoring* any aspect of a debtor's business. Likewise, a secured creditor can become involved in *occasional and discrete financial decisions* relating to the protection of its security interest without incurring liability.

901 F.2d at 1557-58 (emphasis added). One of the few, if not the only, hints the court gave regarding what the

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[1] The College respectfully suggests the absence of such perceived ambiguity.

particular terms used in its new standard mean is found in the first sentence of footnote 13 on p. 1559 of the opinion,[2] and it is as undefined as the phrase "capacity to influence" is itself.

Respondent contended that Fleet was liable for response costs as either a "present owner and operator of the facility," relying on 42 USC §9607(a)(1), or as the owner or operator of the facility at the time the wastes were disposed of, relying on 42 USC §9607(a)(2). The court rejected the claim for liability as a "present owner and operator," applying rules of statutory construction and concluding that imposing liability on this basis would "torture the plain statutory meaning." *Fleet*, 901 F.2d at 1555. Curiously, the court views the statute as having "plain . . . meaning" and also labels it "ambiguous."

Nevertheless, the Eleventh Circuit proceeded to engage in just such a torture of plain statutory meaning when it concluded that liability could arise under 42 USC §9607(a)(2) for a secured creditor, *without being an operator*, by "participating in the financial management of a facility to a degree indicating a capacity to influence the corporation's treatment of hazardous wastes." *Fleet*, 901 F.2d at 1557. As the Petitioner properly acknowledges in its petition, the decision below creates a "new class" of liable parties under §9607(a)(2), a class which does not require any participation in day-to-day operations of a

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[2] "Generally, the lender's capacity to influence a debtor facility's treatment of hazardous waste will be inferred from the extent of its involvement in the facility's financial management." 901 F.2d at 1559 n.13.

facility, but instead merely depends on participation in "financial management" to a degree indicating a capacity to influence how hazardous wastes will be treated, and a class unsupported by the statutory provisions of CERCLA or by its legislative history.

Fleet does not even purport to require a secured creditor to be an "operator" before it could incur §9607(a)(2) liability. Instead, liability allegedly is created by participation in the financial management of a facility. The opinion makes clear that liability does not depend on involvement in the "day-to-day" operations of a facility, nor does it require that the secured creditor participate in management decisions relating to hazardous waste. Instead, the court decides that liability can arise for a secured creditor "if its involvement with the management" of a facility is "sufficiently broad to support the *inference* that it *could* affect hazardous waste disposal decisions *if it so chose.*" *Fleet*, 901 F.2d at 1558 (emphasis added). In doing so, as the Petitioner aptly points out, the court "turns the statute on its head by using the exemption to subject lenders to liability rather than to shield lenders from liability."

Notwithstanding the lack of legislative support for this tortured construction, the court contends that such construction is warranted by legislative history, noting particularly the remarks of Representative Harsha, who introduced the exemption:

> This change is necessary because the original definition inadvertently subjected those who hold title to a . . . facility, but do not participate

> in the management or operation *and are not otherwise affiliated* with the person leasing or operating the . . . facility, to the liability provisions of the bill.

Fleet, 901 F.2d at 1558 n. 11 (citing Remarks of Rep. Harsha, *reprinted in* 2 Senate Comm. on Environmental and Public Works, 97th Cong., 2d Sess., 2 *A Legislative History of the CERCLA* 945 (Comm. Print 1983)) (emphasis in original).

But the court's interpretation overlooks the conjunctive *"and,"* and instead appears to read the explanation as if it were *"or"* The opinion suggests that the use of the word "affiliated" creates a lower threshold for secured creditor liability. Nothing in its history supports the court's conclusion that CERCLA liability for a secured creditor can arise solely through an inference that the creditor could affect hazardous waste disposal decisions if it so chose.[3]

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[3] The opinion also neglects other statutory history of the secured creditor exemption, noted in *Maryland Bank & Trust Co.*, 632 F.Supp. at 579-80, and recently reiterated in *United States v. Nicolet, Inc.*, 712 F.Supp. 1193, 1204 (E.D. Pa. 1989), suggesting that the exemption was only intended to be applicable in those few jurisdictions where a creditor would "hold title" through a deed of trust in order to secure obligations due to it, in contrast to the majority of "lien theory" jurisdictions where the secured creditor possessed only a lien on property and except after foreclosure would never possess any "indicia of ownership." *See generally* H.T. Tiffany, *The Law of Real Property* §1380. If the secured creditor exemption is a basis for "management" and "capability to affect" CERCLA liability where a secured creditor's involvement in a facility's management is "sufficiently broad to support the inference that it

(Continued on following page)

B. The Eleventh Circuit has created a standard for CERCLA liability inconsistent with customary creditors' rights and loan documentation.

The Eleventh Circuit's opinion claims that it was rejecting a literal construction of the secured creditor exemption, urged on it by the government, which would have imposed liability on any secured creditor that participates in any manner in the management of a facility. The basis for this rejection was their belief that to do so would "largely eviscerate the exemption Congress intended to afford to secured creditors." *Fleet*, 901 F.2d at 1556.

Based on experience with a wide array of secured transactions, and with the documentation associated with those transactions, as well as the loan administration growing out of those transactions, the College believes that the Eleventh Circuit's creation of potential CERCLA liability by measuring, through inference, a creditor's capability to affect hazardous waste disposal decisions, results in an even greater evisceration of the exemption.

Most secured transactions involve numerous documents. While the specific instruments will vary from jurisdiction to jurisdiction, and will also change according to the underwriting policies of the lenders involved, it is not at all unusual for most loan agreements, mortgages, lease assignments, deeds of trust and similar

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could affect hazardous waste disposal decision if it so chose," does this mean that there could be no such liability in any "lien theory" state?

instruments to authorize the creditor to approve the tenants and leases with tenants, to make further advances or disbursement of loan proceeds where the creditor determines that there is a lien claim, tax deficiency or other situation jeopardizing the creditor's secured position, or refusing to advance further loan proceeds if a borrower is in default of covenants and warranties made at the time the loan began.

The College believes that such provisions give creditors the opportunity to affect hazardous waste disposal decisions. For instance, certain types of tenants, such as dry cleaning establishments, photo finishing labs or pharmacies can generate solvent and other toxic waste residues which require disposal. Because of the creditor's right to approve tenant selection and lease terms, some lenders have adopted policies precluding such tenants from participation in a borrower's project. In other instances, the lenders have required strict lease terms, together with documentation or reports to both the borrower and its creditor demonstrating that such tenants are properly disposing of the hazardous waste materials used in their operations. Clearly, to the extent that a creditor is controlling the presence of such tenants and demanding the procedures they will follow in order to assure their compliance with environmental requirements, a creditor has the capability to affect hazardous waste disposal decisions. Indeed, routine loan administration decisions, at least indirectly, demonstrate that secured creditors already participate in the financial management of their borrowers.

Similarly, when a borrower encounters an unexpected contingency on a project, be it a subcontractor cost

overrun, an additional tax lien, or a newly discovered underground tank or old petroleum spill, frequently the borrower comes back to its lender and seeks authorization either to fund such claims from loan proceeds or seeks a modification or additional advance of the loan to cover these unexpected contingencies. Traditional loan documentation gives lenders the right to respond to such requests, and in so doing, at least according to the Eleventh Circuit standard, thereby gives those creditors the capability to affect hazardous waste disposal decisions.

The College is unaware of any way to document the number of instances where creditors' financing documentation creates this capability, or to document the myriad of occasions when it may be exercised. It is clear to the College that if participation in "financial management" of a facility, coupled with a "capacity to influence" treatment of hazardous wastes, is to be the test for secured creditor CERCLA liability, virtually every secured creditor, through reasonable loan documentation and loan administration, now is denied the benefits of the secured creditor exemption. CERCLA's legislative history regarding this exemption does not indicate that Congress intended such a result.

II. THE ELEVENTH CIRCUIT'S DECISION HAS APPLIED A STANDARD FOR HAZARDOUS WASTE LIABILITY THAT DIRECTLY CONFLICTS WITH ESTABLISHED CASE LAW AND WITH THE REASONABLE EXPECTATIONS OF LENDERS AND BORROWERS BASED ON THAT LAW.

The decision below will have a significant impact on secured lending. The nation's lenders, including banks

and institutions which lend to businesses, were already extremely wary of potential CERCLA liability, notwithstanding their resisting foreclosing on non-performing loans and not participating in the management of the borrower's business. Now, not only the nation's traditional lenders, but corporate fiduciaries and agencies of the Federal Government, including the Federal Deposit Insurance Corporation ("FDIC") and the Resolution Trust Corporation ("RTC") are concerned with the availability of CERCLA's secured creditor exemption.

Before the Eleventh Circuit's decision, as a result of cases set out in both the district court and Eleventh Circuit *Fleet* decisions, there had been a limited, but clear, construction of the operational liability of a secured creditor. Through decisions such as *Maryland Bank and Trust Co.* and *Guidice*, the statutory exemption language had been construed to mean that, prior to foreclosure, a secured creditor would be exempt from CERCLA liability so long as the secured creditor did not participate in managerial and operational aspects of a facility.

Mirabile was the first case to suggest this interpretation, in 1985. There, the Eastern District of Pennsylvania relieved some secured creditor defendants of CERCLA liability because their participation in the affairs of a facility was "limited to participation in financial decisions," explaining:

> participation which is critical [to CERCLA liability] is participation in operational production, or waste disposal activities. Mere financial ability to control waste disposal practices . . . is not . . . sufficient for the imposition of liability.

Mirabile, slip op. at 3-4.

Prior to *Fleet,* there was little question that a lender could provide financial assistance and isolated instances of management advice without triggering CERCLA liability, so long as it did not participate in the day-to-day management either before or after the business shut down.

The Eleventh Circuit opinion noted cases from the Eastern District of Pennsylvania (*Mirabile*), the Southern District of Texas (*Coastal Casting Service v. Aron,* No. H-86-4463 (S.D. Tex. April 8, 1988)), the Northern District of Illinois (*Rockwell International v. I.U. International Corp.,* 702 F.Supp. 1384 (N.D. Ill. 1988)), the District of Delaware (*United States v. New Castle County,* 727 F.Supp. 854 (D. Del. 1989)), the Southern District of Georgia (*United States v. Fleet Factors Corp.,* 724 F.Supp. 955 (S.D. Ga. 1988)), and the Western District of Pennsylvania (*Guidice*). All of these district courts have applied a standard which creditors have come to rely upon in their loan administration practices. The number of transactions documented accordingly is immense.

In the five years since the standard was first articulated in *Mirabile,* lenders have adjusted their loan administration practices to this requirement. In doing so, they have sought to avoid becoming involved in the operational affairs of their borrowers. Lenders had come to believe that they were complying with what was necessary to avoid CERCLA liability, absent foreclosure and actual participation in the day-to-day operation of their borrowers.

But the Eleventh Circuit rejected that test as "too permissive" and created a new standard by which

availability of the exemption is to be judged. The new test presents secured creditors with even more uncomfortable dilemmas than they had before *Fleet*. If they elect to foreclose on a troubled property, they risk direct liability for the cleanup, without regard to fault, as well as the loss of their investment in the property. If they shy away from this risk, they are transformed into unsecured status for all intents and purposes and may still be liable for cleanup costs. Customarily, at the outset of the loan process, a creditor considers whether to put in protections, such as periodic policing of activities, to ensure that a hazardous waste condition would not arise and, if a condition did arise, that it would not continue. In light of *Fleet*, the mere inclusion of such protections could render a creditor liable. Understandably, creditors will be hesitant to police the activities of their debtors. By deciding not to police the activities of their debtors, creditors risk pollution of their secured interest. Given the decision in *Fleet*, creditors will be less likely to opt to work out the loan, not wishing to risk liability under *Fleet* by further involvement with the property. In many cases, taking steps to foreclose will result in bankruptcy. The effect will be disastrous on an already troubled national economy.

The central issue in *Fleet* became whether the lender could be held liable on any correct reading of the secured creditor exemption for its action after the borrower ceased operations but before the lender foreclosed its interests in the borrower's inventory and equipment. The United States Environmental Protection Agency ("EPA") argued that Fleet participated in the management of the facility and was therefore liable as an owner or operator. EPA alleged, *inter alia*, that Fleet required the borrower to

seek its approval before shipping its goods to customers; dictated when and to whom the finished goods should be shipped; controlled access to the facility; and contracted with the auctioneer to dispose of the fixtures and equipment at the borrower's facility. EPA also alleged that Fleet should be liable for conduct during and after the auction sale, alleging that friable asbestos was knocked loose from pipes during the auction or when the unsold goods were subsequently removed. The Eleventh Circuit held that, if proved, such activities made Fleet liable because "Fleet's involvement in the financial management of the facility was pervasive, if not complete." *Fleet*, 901 F.2d at 1559.

Even, *arguendo*, if Fleet's involvement in the financial management of the facility was pervasive, if not complete, Congress never intended the participation in management aspect of the exemption to be activated unless there was some nexus between the activities and the causing or failure to abate the contamination giving rise to CERCLA liability in the first instance. The mere fact that a secured creditor seeks to protect its security interest by monitoring, albeit in depth, the activities of its debtor so as to mitigate its losses when the loan's performance becomes seriously in doubt or non-existent, should not transform such activities into CERCLA liability for one who has neither caused or facilitated nor failed to abate the existence of hazardous substances on a site involved in a secured credit transaction.

Indeed, the facts in *Fleet* were such that the court below could have said that Fleet participated in management sufficiently to lose the exemption, without announcing its new radically expansive standard (by which to

make such determinations) by dramatically lowering the threshold of participation in the borrower's affairs that may safely be exercised by a lender. The circuit court could have readily found Fleet potentially liable as a prior *operator* during the winding down period by applying the *Mirabile* standard. But the court held: "We . . . specifically reject the formulation of the secured creditor exemption suggested by the district court in *Mirabile*." *Fleet*, 901 F.2d at 1558. *Mirabile* had suggested that activities, such as determining the order in which customer orders were to be filled, demanding additional sales from a facility, supervising operations of a facility, and assisting in certain manufacturing changes or personnel reassignments, could bring a secured creditor outside the protection otherwise available under the exemption.

Instead, the court below adjudged Fleet potentially liable because it "participated in management" sufficiently to lose the exemption. If the participation in management bears no significant relationship or has no essential nexus to the activities CERCLA proscribes, and the *Fleet* test is couched in such imprecise phraseology as "inference," "could" and "if it so chose," there is literally no threshold regarding what a secured creditor can engage in with any degree of safety in order to avail itself of the congressional exemption.

At least Judge Kozinski, speaking for the Ninth Circuit in *Bergsoe*, limited the management activities to actual rather than ephemeral. At least "actual" connotes a close nexus between the proscribed activity and the so-called management that bears on the proscribed activity. As the *Bergsoe* court stated, "Merely having the power to

get involved in management, but failing to exercise it, is not enough." *Bergsoe*, 910 F.2d at 673 n.3. Judge Kozinski also held, "What is critical is not what rights the Port had, but what it did." *Id.* at 672. And, importantly, Judge Kozinski specifically recognized the nexus concept when, speaking for the *Bergsoe* panel, he stated:

> . . . we hold that a creditor must, as a threshold matter, exercise actual management authority before it can be held liable for action or inaction *which results in the discharge of hazardous wastes.*

Id. at 673 n.3 (emphasis added).

Certainly, *Fleet* and *Bergsoe* are in clear conflict – conflict that this Court needs to resolve so that ongoing secured loan transactions may proceed, and without undue interruption.

The Eleventh Circuit's opinion creates secured creditor CERCLA liability through an inference based on some degree of involvement with management of a facility. By contrast, the Ninth Circuit emphasized actual involvement and held that "there must be *some* actual management of the facility before a secured creditor will" become liable. *Bergsoe*, 910 F.2d at 672.

Subparagraph .1(a) of Rule 10 of the Rules of this Court could not have envisioned a more obvious conflict between decisions of different United States courts of appeals. Moreover, pursuant to subparagraph .1(c) thereof, " . . . a United States court of appeals has decided an important question of federal law which has not been, but should be, settled by this Court . . . "

CONCLUSION

For the "special and important reasons" set forth above, the American College of Real Estate Lawyers respectfully urges this Court to grant the Petition for Writ of Certiorari and review the decision of the United States Court of Appeals for the Eleventh Circuit.

DATED: October 19, 1990.

Respectfully submitted,

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